

## Internal Revenue Service

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Department of the Treasury  
Washington, DC 20224

Third Party Communication: None  
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Person To Contact:  
, ID No.

Telephone Number:

Refer Reply To:  
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PLR-141469-11  
Date: October 19, 2011

### LEGEND

Company =

State =

Trust1 =

Trust2 =

Date1 =

Date2 =

Date3 =

Date4 =

Date5 =

Date6 =

Dear :

This letter revokes and replaces private letter ruling 201128023, dated March 17, 2011, issued to Company because it contained an error. This letter responds to a letter dated December 20, 2010, and subsequent correspondence submitted on behalf of

Company by its authorized representative, requesting a ruling under § 1362(f) of the Internal Revenue Code.

### FACTS

Company incorporated in State on Date1, and elected to be an S corporation effective Date2. Trust1 and Trust2 were formed and received all the shares of Company on Date2. Trust1 and Trust2 (collectively "Trusts") each made an election to be treated as an Electing Small Business Trust ("ESBT"), but, due to inadvertence, the ESBT elections included an effective date of Date3, and erroneously stated that Trusts acquired Company's stock on Date4. The ESBT election for Trust2 also listed an erroneous potential current beneficiary. Trusts did not otherwise qualify as eligible shareholders of an S corporation as of Date2. As a result, Company's S corporation election was not effective as of Date2.

On Date5, the trustee of Trust2 died. As of Date5, Trust2 became a foreign trust because of the appointment of a foreign trustee. On Date6, Trust2 replaced its foreign trustee with a United States trustee that would make Trust2 a domestic trust and eligible to be an ESBT.

Company represents that it intended to make its S corporation election effective as of Date2 and that the failure to file correct ESBT elections was inadvertent and not motivated by tax avoidance or retroactive tax planning. Company further represents that there was no intent to terminate Company's S corporation election and that appointment of a foreign trustee was inadvertent and not motivated by tax avoidance or retroactive tax planning. For all relevant taxable years, Company and Company's shareholders' filed their federal income tax returns consistent with Company qualifying as an S corporation, and Trusts have filed consistent with Trusts having valid ESBT elections in effect since Date2. In addition, Company and Company's shareholders agree to make any adjustments consistent with the treatment of Company as an S corporation as may be required by the Secretary with respect to the period specified by § 1362(f).

### LAW

Section 1361(a) provides that the term "S corporation" means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for such year.

Section 1361(b)(1) provides, in part, that the term "small business corporation" means a domestic corporation which is not an ineligible corporation and which does not have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual.

Section 1361(c)(2) provides that certain trusts, such as ESBTs, are permitted as shareholders of an S corporation.

Section 1361(c)(2)(A) provides, in part, that § 1361(c)(2) shall not apply to any foreign trust.

Section 1361(e)(1)(A) provides that for purposes of § 1361, except as provided in § 1361(e)(1)(B), the term “electing small business trust” means any trust if - (i) the trust does not have as a beneficiary any person other than an individual, an estate, an organization described in § 170(c)(2), (3), (4), or (5), or an organization described in § 170(c)(1) that holds a contingent interest in the trust and is not a potential current beneficiary; (ii) no interest in the trust was acquired by purchase; and (iii) an election under § 1361(e) applies to the trust.

Section 1362(a) provides that, except as provided in § 1362(g), a small business corporation may elect, in accordance with the provisions of § 1362, to be an S corporation.

Section 1362(d)(2)(A) provides that an election under § 1362(a) will be terminated whenever (at any time on or after the first day of the first taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation.

Section 1362(d)(2)(B) provides that the termination shall be effective on and after the date of cessation.

Section 1362(f) provides, in part, that if (1) an election under § 1362(a) by any corporation was not effective for the taxable year for which made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents, or was terminated under § 1362(d)(2) or (3) or § 1361(b)(3)(c), (2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent, (3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness or termination, steps were taken (A) so that the corporation for which the election was made or the termination occurred is a small business corporation or (B) to acquire the required shareholder consents, and (4) the corporation for which the election was made or the termination occurred, and each person who was a shareholder in such corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such ineffectiveness or termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.

Section 1.1362-4(d) of the Income Tax Regulations provides that the Commissioner may require any adjustments that are appropriate. In general, the adjustments required should be consistent with the treatment of the corporation as an S corporation or QSub during the period specified by the Commissioner. In the case of stock held by an ineligible shareholder that causes an inadvertent termination or invalid election for an S corporation under section 1362(f), the Commissioner may require the ineligible shareholder to be treated as a shareholder of the S corporation during the period the ineligible shareholder actually held stock in the corporation. Moreover, the Commissioner may require protective adjustments that prevent the loss of any revenue due to the holding of stock by an ineligible shareholder (for example, a nonresident alien).

### CONCLUSION

Based solely on the representations made and the information submitted, we conclude that Company's S corporation election was ineffective as of Date2 due to the failure to file proper and timely ESBT elections for Trusts. We conclude that the ineffectiveness of Company's S corporation election was inadvertent within the meaning of § 1362(f).

In addition, assuming Company's S corporation election had been properly in effect, it would have terminated on Date5 because of Trust2 becoming a foreign trust and an ineligible shareholder of an S corporation. We conclude that such a termination would have been inadvertent within the meaning of § 1362(f).

Accordingly, under § 1362(f), Company will be treated as an S corporation from Date2, and thereafter, provided that Company's S corporation election is otherwise valid and is not otherwise terminated under § 1362(d).

This ruling is contingent on Company and its shareholders treating Company as having been an S corporation for the period beginning Date2, and thereafter. This ruling is also contingent on the trustees of Trusts filing valid ESBT elections, effective Date2, with the appropriate service center within 120 days of the date of this letter. Provided that the ESBT elections are made, from Date2, and thereafter, Trusts will be treated as ESBTs effective Date2. A copy of this letter should be attached to the elections. In addition, this ruling is contingent on Trusts and their beneficiaries treating Trusts as ESBTs from Date2, and thereafter. If these conditions are not met, then this ruling is null and void.

Except as expressly provided herein, we express or imply no opinion concerning the federal tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, we express or imply no opinion concerning whether Company is otherwise eligible to be an S corporation for federal tax purposes or whether the Trusts are otherwise eligible to be ESBTs.

This ruling letter is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Under a power of attorney on file with this office, we are sending a copy of this letter to Company's authorized representative.

Sincerely,

James A. Quinn  
Senior Counsel, Branch 3  
Office of the Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosures (2)  
Copy of this letter  
Copy for Section 6110 purposes